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EMPLOYEES VS INDEPENDENT CONTRACTORS – OLD CONCEPTS IN NEW LEGISLATION CLOTHING

The new definition of employment introduced into the* Fair Work Act 2009 *(Cth) (FW Act) by the* Fair Work Legislation Amendment (Closing Loopholes No. 2) Act 2024 *is expected to take effect on 26 August 2024. Despite constituting a significant legislative reform, the new definition imports some old concepts developed by courts that will inform how the provisions are to be interpreted. In this update, we chart the development of the test for distinguishing employees from independent contractors and provide guidance on steps businesses should take to ensure that their working relationships are characterised appropriately.

In this update, we discuss significant changes to the characterisation of employment relationships under the FW Act. One of those changes is that, for the first time, the FW Act will contain a comprehensive statutory definition of 'employee', which will be found in section 15AA.

Despite the novelty of the provision, it relies on concepts developed by courts to determine whether a relationship is one of employee or independent contractor. This presents a useful juncture to look back on the development of the employee/independent contractor dichotomy, before looking forward at what the reforms mean for businesses who engage labour.

The historical approach: the multifactorial test

The courts developed the 'multifactorial test' for determining whether an individual was properly characterised as an employee or independent contractor. The application of that test involved asking a series of questions about the "totality of the relationship" between the relevant parties and weighing each indicium to produce an overall result: employee or contractor. The most important factor was control (or lack of control) exercised over an individual, as this is the hallmark of a contract *of service* (i.e. a contract of employment).

Evidence of each of the factors was determined not only by reference to the contract between the parties, but by how they conducted the relationship in practice. The exercise was often an impressionistic or intuitive one engaged in by looking back on the relationship as it could morph over time. The application of that exercise became unwieldy as the scope of the enquiry looked at the entire working relationship, not only the arrangement the parties entered into on commencement.

Personnel Contracting and *Jamsek*

The High Court of Australia disavowed the roving enquiry into the working practices of the parties to a relationship in *CFMMEU v Personnel Contracting Pty Ltd* (***Personnel Contracting***)[1] and *ZG Operations Australia Pty Ltd v Jamsek* (***Jamsek***).[2] Instead, it made the characterisation of the relationship dependent on the nature of the legal relationship created by the contract between the parties, with reference to their respective *legal* rights and duties under that contract, allowing the subsequent conduct of the parties in carrying out their relationship to be considered only in limited situations (being in circumstances where the contract is a sham, it has been varied, its terms have been waived or subject to an estoppel). This change meant that the multifactorial test was confined narrowly to, essentially, the terms of the contract.

[1] [2022] HCA 1.

[2] [2022] HCA 2.

Back to the future

Section 15AA of the FW Act, which takes effect later this year, was expressly enacted in response to *Personnel Contracting* and *Jamsek*. It provides that for the purposes of the FW Act, the ordinary meaning of employee and employer is determined by ascertaining "*the real substance, practical reality and true nature of the relationship*" between the parties. This requires a court to consider the "*totality of the relationship*", including by reference to not only the terms of the contract governing the relationship, but other factors including how the contract is performed in practice.

The legislation picks up the language of the pre-*Personnel Contracting/Jamsek* approach to the multifactorial test, in effect reviving the old law in this space.

Based on those previous decisions, we can expect that the courts will have regard to factors including, but not limited to:
• the degree of control exercised by the employer/principal over the employee/independent contractor; • the mode of remuneration; • the provision and maintenance of equipment; • the obligation to work; • the hours of work and provision for holidays; • the deduction of income tax; • the delegation of work by the putative employee. • the right to have a particular person do the work; • the right to suspend or dismiss the person engaged; • the right to exclusive service; and • the right to dictate the place of work, hours of work etc.

What is truly novel about the new provisions is the ability for an individual to "opt out" of them provided their earnings exceed the "contractor high income threshold". The contractor high income threshold is still to be set by regulation, but we can expect some semblance to the "high income threshold" currently used to determine access to the unfair dismissal jurisdiction and guarantees of annual earnings. Under the scheme, an individual may give a one-time "opt out notice" to the principal with the effect that the new provisions won't govern their relationship, and so the common law test in Personnel Contracting and Jamsek will apply instead. The individual may revoke the notice at any time. It remains to be seen whether such notices will have widespread use in practice.

It is important to bear in mind that the new definition of employment only applies with respect to the FW Act (including with respect to coverage and application of modern awards and enterprise agreements), and provided the relevant individual has not given an opt out notice. The new definition would not apply for the purposes of other laws, such as superannuation or payroll tax legislation.

The laws apply to relationships entered into before the new definition comes into force, as well as relationships entered into afterwards. Any rights, privileges, obligations, or liabilities accrued by an individual before commencement would continue after the new provision commences. However, service-related entitlements are to be determined prospectively – so, for example, if an individual engaged prior to 26 August 2024 was found to be an employee under section 15AA but not at common law, their service-related entitlements, such as their minimum employment period, leave entitlements, etc., would run from 26 August 2024, not the earlier engagement date. In addition, disputes already on foot at the time of commencement would be determined with reference to the historical approach outlined at the start of this article.

Key takeaways

From a practical perspective, businesses will still need to ensure that the services agreements between them and independent contractors accurately reflect the nature of the relationship. For highly paid contractors, businesses should consider building into their processes a means of giving a written notice stating that the individual may provide the business with an opt out notice.

What will be most challenging for businesses is ensuring that an independent contractor relationship does not depart from the written terms of the arrangement over time by adopting work practices that are inconsistent with those terms. This will necessarily be fact-specific, although we anticipate long term contractor arrangements,

arrangements for unskilled and low paid labour, and independent contractors who perform the same work side-by-side employees will be in the spotlight and should be avoided, to the extent possible, by businesses.

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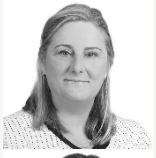

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